

corporate governance and the proxy vote

The increased scrutiny of both regulators and special interest groups within the global investment community has resulted in increased regulation and strong pressure on fund managers to vote all meetings and publicise their votes and associated policies. This is well illustrated by the increased focus resulting from the passage in the U.S. of the Sarbanes Oxley Act of 2002,¹ and the Securities and Exchange Commission rules on proxy voting disclosure, which impacts U.S. registered investment companies and their subsidiaries, and by the recommendations laid out in Paul Myners' report to the Shareholder Voting Working Group² in the U.K. in February 2004.

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As a result of this pressure, global voting levels have increased significantly. Further, the demand to standardise and streamline inefficient global voting practices which affect shareholders' ability to efficiently exercise their right to vote continues to grow.

Today, JPMorgan processes approximately 400,000 global proxy voting ballot instructions from foreign institutional investors per year. Since 2003, there has been an increase of over 100% in the number of agendas generated and a 50% increase in the number of global ballots actually voted.

Because voting practices vary significantly by market, keeping abreast of rapidly evolving corporate governance practices and regulations is a challenge.

Barriers to voting — Share Blocking

Among the biggest frustrations for institutional investors is the requirement for share blocking: one of a number of areas currently under review in the recently published *European Commission Fostering an Appropriate Regime for Shareholders' Rights*.³ If a vote is cast, the share cannot typically be sold until the vote is either revoked or the meeting has taken place.

Since share blocking affects a security's liquidity, a fund must determine a policy on whether to vote at or refrain from voting at a meeting in order to keep the position liquid. Sometimes, the fund manager may decide that liquidity of the position outweighs the value of the vote and may choose not to vote in markets that operate a blocking practice.

An alternative mechanism used by issuers across some markets is a 'record date' system. The record date

provides a cut-off reconciliation date by which settled positions are eligible to participate in the meeting. The record date system is generally preferable to share blocking since it does not block the disposal of shares and guarantees a voting right on a given date, allowing the shareholder to sell or lend their securities. However, a record date can create conflict in markets that do not standardise the timing of a record date or set it too far in advance of the meeting.

Complications may arise in some countries where there is no recognition of a nominee or, there is a distinction between what types of actions a nominee may carry out. The nominee, for example, may be entitled to carry out all rights in regard to clearing and settlement, but may not have the administrative rights in regard to proxy voting. This would require a nominee to segregate client positions to achieve registration in the client's name to enable voting at the company meeting. In addition to segregating the assets, the beneficial owner may also be required to provide the sub custodian, who safe keeps the assets, with a power of attorney authorising the submission of the fund's votes. This process typically results in added end-to-end administrative burden.

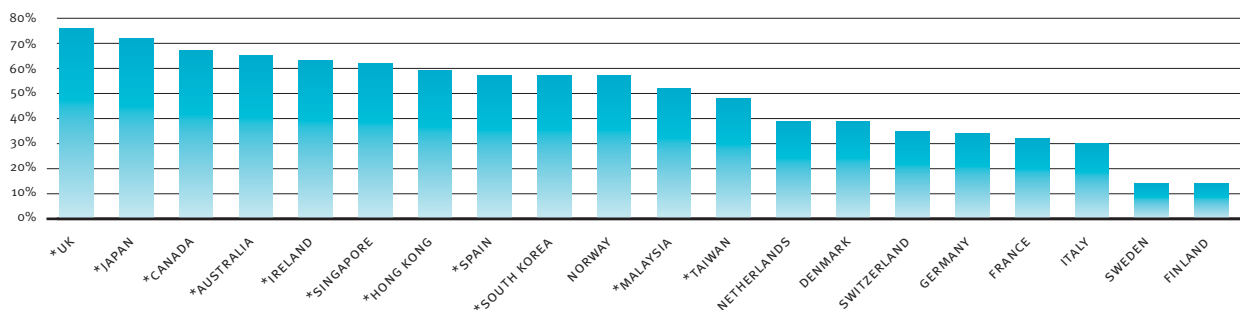
Keys to Improving Participation

Foreign investors are looking for a standard approach that simplifies the proxy voting process, helping reduce or eliminate the conflict between investment returns and corporate responsibility.

The following table notes the average ballot return rate for a selection of markets where JPMorgan offers global voting services. The table demonstrates that markets that offer a straightforward voting model without the need to block shares, register positions in beneficial owner name,



Percent of Ballots Voted Across a Selection



* Markets where there is no requirement to block shares or register in Beneficial Owner name to allow voting

or require Power of Attorneys and or personal representation at a meeting, typically see a much higher percentage of vote execution.

Improving Efficiency

Foreign institutional investors are looking for timely notification of meeting announcements, full disclosure of information and a mechanism to ensure that their vote is received by the company and counted at the meeting. Removal of paper based submissions of the proxy vote and the need for physical representation at meetings ideally facilitated through electronic voting are two of the most significant factors that could help create efficiencies and improve the voting process. Implementation of an electronic voting platform would reduce the risk of votes being lost and bring efficiency to the market through ease of access and improved confirmation of voting to investors across the world.

Electronic voting has been facilitated in the U.S. through the use of third party providers and is reasonably efficient. In the U.K. an example of an electronic voting platform that has been embraced by institutional investors and market participants is the model facilitated by CREST, the central depository. In the past year, more than 200 issuers in the various U.K. indices allowed voting through the platform and it is anticipated that issuer adoption will further increase over the next few years. In addition to facilitating automation and reduced use of paper, the platform also provides institutions and issuers with a much clearer audit trail of votes cast.

Keys to improving participation

In accordance with “best practices” employed around the world, sensible recommendations for increasing shareholder participation might be:

1. Standardise the time by which securities must be registered or shareholders disclosed in order to participate in a company meeting
2. Allow for safekeeping of securities in omnibus accounts with multiple registrations or the potential for separate disclosure
3. Recognition of intermediaries’ and custodians’ contractual relationships with their customers, without the need for powers of attorney
4. Removal of share blocking practices

Corporate Governance is a Responsibility

Good corporate governance is no longer an option but rather the responsibility of all market participants. The fiduciary importance and financial benefits of successfully and properly voting proxies is paramount in exercising shareholder rights. With 24-hour customer service, JPMorgan’s own Proxy Voting Service proactively serves the needs of institutional investors with a high quality cost-effective proxy voting solution, providing full online electronic voting capabilities that help institutional investors exercise their proxies and fulfill their increasingly expanding corporate governance responsibilities (see also *Thought* magazine, Q2/2004).

JPMorgan works both directly and indirectly with various market bodies to promote initiatives and processes that will allow greater participation at company meetings. Earlier this year the firm actively participated in the U.K. shareholder working practice group on the “Review of the Impediments to Voting U.K. Shares”, and more recently has worked with the Danish stock exchange raising some of the barriers foreign investors face in voting Danish securities in discussions with market participants.

By working directly on local market initiatives, or indirectly through international initiatives such as the ICGN,⁴ the firm believes the industry can collectively create a better environment for voting cross border securities. ○○○

For more information on proxy voting or JPMorgan’s Proxy Voting Service, contact your relationship manager or client service officer.

1. The Act, named after its primary architects, Senator Paul Sarbanes (D-Maryland) and Representative Michael Oxley (R-Ohio), is organised into eleven sections. These sections deal with such issues as auditor independence, corporate responsibility, enhanced financial disclosures, conflicts of interest, and corporate accountability, among other things.

2. In response to high profile cases of “lost votes” in the U.K. market, Paul Myners, a leading British reform advocate, was commissioned by the U.K. Shareholder voting Working group to perform a detailed review of the voting process.

3. The European Commission has launched a public consultation exercise of basic shareholders’ rights in company general meetings and solving problems in the cross-border exercise of such rights.

4. The International Corporate Governance Network (ICGN) is a leading authority in corporate governance.